

# The New Practice (TNP)

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## Public-Private Partnership: Drafting Considerations in PPP Contracts

government is the party to make policies, pass laws and implement the same to ensure the car park is used and penalize illegal parking on Risy Cattle Road. Rexy Limited should in turn be responsible for the design, construction, and delivery of the car park. Consequently, Rexy Limited must insure against construction risk to ensure the delivery of the project.

At the negotiation stage, parties must assess the risks being allocated to them to confirm they have control over how those risks could arise and are able to take measures to mitigate or avoid them. This is where improper risk allocation could result in overloading a party with inappropriate risks and lead to project failure. For example, one of the initial challenges with the concession of the Murtala Muhammed Airport II was the Federal Government's inability to compel off-takers and end user patronage of the project's services. Although this issue relates to the commercial success of the project and was a risk to be borne by the private partner, such a risk should fall within the powers of the government party to compel the use of the service. This is therefore illustrative that risk allocation is not necessarily a question of the nature of the risk, but who has better control over the risk in question.

### Fees

While the primary objective of the private party in any PPP contract is profit, the government party is more interested in the welfare of her citizens and the easy accessibility of the services to be rendered by the project. One of the best ways to achieve this objective is by charging fees reflective of the cost of the services provided by the project. Fees charged in a PPP project should take the following into account: parties' contributions; the project term; the parties' profit expectations; revenue split; price control; and Foreign Exchange (FX) issues.

Depending on the project model, it is imperative to limit the fees end users will pay to have access to the services. As earlier mentioned, the essence of PPP arrangements is to cater for the needs of the citizens and if this is defeated by unreasonable pricing, it defeats the purpose. That said, parties should agree on a reasonable pricing mechanism, identifying contemplated issues such as inflation, and a third party pricing arbiter/regulator to balance things out where both parties are unable to agree on proposed increase in pricing.

Parties that are unable to adjust prices at a speed and to a level to reflect changes in project costs, may find themselves without a project to run. Therefore, while it is imperative to charge fees that reflect the public nature of the project, the PPP contract must have clear provisions responsive to cost escalation, allowing for cost recovery, profit and usage of the services.

The government party should also avoid signing a PPP that could result in political backlash. A good example was the proposed toll increase at the Lekki-Epe toll which led to public outcry. Services provided by government projects are generally assumed to be free or at the fairest prices. Consequently, the government party must be careful not to negotiate a deal that may make it lose trust with its people.

### Termination

It is instructive for parties to critically consider the issues that may result in terminating their deal. They must also ensure they clarify the rights of the innocent party to terminate and remedies available upon termination. As we are in the season of elections, "Political Risk" comes directly to mind, and thus it is essential to mention both parties must guard against the unilateral termination of a PPP contract by a present or succeeding administration. Parties must essentially make reneging on the deal extremely unattractive without justifiable cause. Accordingly, negotiating considerations should give room for continuity, to avoid the project crashing in the event of undue termination or takeover by a new government. Parties may want to provide adequate time for handing over the project, the project equipment or the provision of the services in the event of termination. In essence, this should help avoid the project being halted abruptly or putting it in disarray upon termination.

In addition, parties should clearly provide for liquidated damages to avoid a situation where a party is left without his shirt, after achieving critical milestones in the project, and to discourage breaches of any form. Here, the private party may consider including a waiver of a sovereign immunity clause in their agreement. The government party on the other hand may include clauses to cater for the performance failure, capacity failure after a stipulated timeframe, and failure to build the project to the satisfaction of the public party.

### Dispute Resolution

It is advisable to consider a dispute resolution procedure reflective of the cost and profile of the project. The primary consideration should be cost, speed, forum, jurisdiction and impartiality, bearing in mind that PPP contracts are commercial transactions.

In deciding forum, parties should consider the cost implication of their preferred institution. For example, where the parties opt for arbitration as preferred dispute resolution mechanism, this would involve higher financial implications as opposed to the traditional courtroom forum. Other things to bear in mind include the number of the arbitral tribunal, the exact arbitration forum, the jurisdiction, and the enforcement of decisions of the tribunal.

### Events of Default

Events of default are another key consideration parties must contemplate and provide for. It is critical to accommodate situations where a party who is unable to carry out its obligations under the PPP agreement may be granted concessions to enable the defaulting party remedy any breach committed. These remedies should include the period to notify the other party of an impending breach, proposal to remedy such breach and the timeline for remedying the breach.

### Lenders Rights<sup>1</sup>

Most concessions involve huge financing with recourse to external funding. With this in mind, concession negotiations must be open to considering the concessionaire's funding obligations and project continuity. Parties must assess and make sufficient provision for the lending obligations and the lenders' rights. It is also necessary to separate the lenders' rights from the project itself, such that the project cannot stand as security for any loan taken. Also, parties must critically examine and define a lender's "step-in rights".<sup>1</sup> It is important to ensure the lender can only step into the exact shoes of the concessionaire and is not able to alter the initial arrangements between the parties or disrupt the project.

### Conclusion

Nations should thrive with the help of PPPs, as governments barely have full capacity, funds, and technical know-how to carry out these projects to adequately provide the much needed facilities and amenities for her citizens. That said, a great PPP starts and ends with a properly negotiated contract reflective of the parties' rights, obligations and benefits to the public. Whilst the success of a PPP project is largely dependent on several other factors outside parties' negotiations, ensuring these critical elements mentioned above are considered, examined and provided for, is a good start to achieving the intended objective.

<sup>1</sup>This is a right of the lender to "step in" by replacing the concessionaire (its borrower) where the concessionaire is unable to meet its financing obligations to the lender

It is no news that the construct and adoption of Public-Private Partnerships (PPP) across governments around the world has been geared towards solving respective infrastructural deficits coming from constantly expanding obligations. Nigeria is no exception to this, as she has embarked on a number of infrastructure projects using the PPP model.

In its most simplistic form, PPPs are long-term funding arrangements between governments and private sector partner(s) to provide public goods and services traditionally carried out by governments. While a government's primary motivation in embarking on a PPP is the provision of public goods and services at the best value, the private party's primary motivation is maximizing profit. Consequently, PPPs are a constant negotiation playing field, where risk assessment, mitigation and allocation are the parties' contending objectives. Accordingly, negotiating the terms of a PPP project requires an effective blend of analytical, negotiation and good draftsmanship skills, to provide a working document for an adequate protection of parties' interests, and to achieve a common goal for the public at large.

### What are the Key Provisions to Consider when Negotiating PPP Contracts?

#### Risk Allocation

Risk allocation continues to be the most critical element in negotiating these contracts. This simply requires you deciding which party will bear the cost (or reap the benefit) of a change in project outcomes arising from each risk factor. Risk is therefore allocated to the party who is best able/suited to manage the particular risk. For example, any risk associated with the physical integrity of a piece of infrastructure built under a PPP model should ideally be allocated to the party carrying out the construction.

In the process of negotiating the contract, the parties must allocate risks and state the extent of risk each party should bear. The structure of PPP contracts also mean that the party bearing a particular risk is incentivized to devise means of avoiding the risk or mitigating the impact of such risks, should they occur. For context, where Chinonye State concedes the development of a multi-story car park to Rexy Limited (the private party) to reduce the incessant and indiscriminate parking on the Risy Cattle Road, the risk associated with land acquisition, compensation, and ensuring public patronage should ideally be placed with Chinonye State government. This is because Chinonye State

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A great PPP starts and ends with a properly negotiated contract reflective of the parties' rights, obligations and benefits to the public.”

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